BRIEF IN SUPPORT OF PETITION.

THE JURISDICTION INVOKED.

The jurisdiction to grant the writ of *certiorari* is invoked under §240 (a) of the Judicial Code as Amended by the Act of February 13, 1925 (43 Stat. 1938, 28 U. S. C. A. §347). The order of the United States Circuit Court of Appeals became final on September 4, 1942 when the petition for rehearing was denied (R. 179).

OPINIONS BELOW.

The District Court rendered its decision on February 26, 1942 (R. 129). Its opinion is reported in 43 Fed. Sup. 37. The Circuit Court of Appeals rendered its decision on August 4, 1942 (R. 152). Its opinion was reported in 130 Fed. (2) 300.

STATEMENT OF THE CASE.

In addition to the statement of the case given in the petition which is adopted here by reference, it should also be stated that the suit was originally brought by three other plaintiffs and the petitioner was subsequently joined as an additional party plaintiff. The entire suit was dismissed for want of jurisdiction and on review it was reversed as to the petitioner who remained as the only plaintiff (117 Fed. (2) 95; *certiorari* denied 313 U. S. 559). After the reversal, respondents filed their answer (R. 11). Plaintiff obtained answers to interrogatories and admissions from the defendants (R. 127), and the respondents took plaintiff's deposition (R. 51). Thereafter,

respondents moved for a summary judgment (R. 14) based on the depositions (R. 51) and their affidavits (R. 15, 36, 47).

Another noteholder (Grace W. York) who did not accept the terms of the offer and who was joined as a plaintiff was also dismissed as a party (117 Fed. (2) 95) and she, therefore, filed a class suit on behalf of the holders of $1,213,000 of notes who did not accept the offer and did not receive anything out of the "segregated assets" or "assigned securities". A copy of the complaint appears in this record at page 168. This suit is still pending but may be defeated as a result of the opinion in the instant case as pointed out in the petition for rehearing (R. 164).

The $30,000,000 note issue and the "offer" were also the subject matter of an investigation by the Senate Committee and is reflected in its Report, Part 3, No. 714 of the 77th Congress. This report was printed subsequent to the rendition of the opinion by the District Court but before the entry of the final judgment. We forwarded a copy of this printed report to the court with a request that it grant a rehearing but the District Court entered the final order without making that report a part of the record. We attempted to make this report a part of the record by a motion in the United States Circuit Court of Appeals but the court denied the motion (R. 153). It is our contention that the District Court, the Court of Appeals, as well as this Court may take judicial notice of the official report of the Senate Commission without making that report a part of the record.*

* See Senate Report No. 714, Part 3, relating to the "1931 crisis" which resulted in the "offer" manipulated by the respondents and the argument under Point V (pp. 44-45, infra).

SUMMARY OF ARGUMENT.

I. The affirmance of the summary judgment on the ground that no action for breach of trust was maintainable by the beneficiary of the trust against the Trustee because no trust relationship was established in the absence of a trust *res* in the possession of the Trustee, is a departure from the general law relating to trusts, and the decision is not in harmony with the well accepted principles relating to duties of trusts and fiduciaries.

II. The affirmance of the summary judgment on the ground that even if there existed a trust relationship plaintiff failed to show even *prima facie* that she sustained any loss as a result of the breach of trust because the assets of the company were of doubtful value, is in direct conflict with another decision of the same Circuit in construing Rule 56 that every doubt must be resolved against the movant.

III. The respondents were guilty of fraud and violated their trust duties and under no theory of law was it proper to sustain their motion for a summary judgment under Rule 56.

IV. The fraudulent offer to exchange was not the offer of the Van Sweringens but the offer of the respondents, Morgan and Guaranty Trust Company, and it is they who committed the fraud and breach of trust.

(a) Where an agent perpetrates a fraud on a third party for the benefit of his undisclosed principal, the third party may sue the principal upon the disclosure.

(b) Even if the offer was that of the Van Sweringens the defendants who ratified the offer and accepted the benefits therefrom are liable.

(c) The fact that neither Morgan nor Guaranty Trust personally defrauded the plaintiff is no defense.

(d) The real purpose of the offer was to avoid the collapse of the Van Sweringen empire wherein Morgan and the Guaranty Trust Company were personally interested and not to save the investment of the noteholders.

(e) It was the duty of the Trustee to protect the interest of the noteholders which it failed to do because of its adverse interest.

V. Federal courts may take judicial notice of official reports of Congressional Committees, and the official report of the Congressional Committee conclusively demonstrates the fraud, the violation of the trusts, and the damage sustained.

ARGUMENT.

I.

The Affirmance of the Summary Judgment on the Ground That No Action for Breach of Trust Was Maintainable By the Beneficiary of the Trust Against the Trustee Because No Trust Relationship Was Established in the Absence of a Trust Res in the Possession of the Trustee Is a Departure from the General Law Relating to Trusts and the Decision Is Not in Harmony With the Well Accepted Principles Relating to Duties of Trusts and Fiduciaries.

The statement of the Court of Appeals (R. 156) that the suit for a breach of trust was not maintainable because no trust was established by the trust indenture and that "Actually the trust indenture securing the notes and naming the Guaranty Trust Company trustee was no such thing" is based on a clear misconception of the law of trusts and the accepted principles governing rights and duties of fiduciaries.

The Trust. In concluding that there was no trust relationship between the Trustee and the noteholders the Court of Appeals overlooked important provisions of the Trust Indenture and applicable principles relating to the law of trusts. The Trust Indenture was executed by the trustee, which affixed its corporate seal "**in evidence** of its acceptance of the **trusts**", thereby "**created**" (R. 104). The notes were certified by it "as Trustee" (R. 79) and the issue was limited to such amounts as may be "delivered to the trustee for authenti-

cation" (R. 80). The issuer was prohibited from mortgaging or pledging its assets and from disposing of any of its cash under certain conditions (R. 82). There was a provision for "segregated assets" and "assigned securities" and the execution of a simultaneous agreement to be delivered "to the Trustee" relating to the performance of the provisions for the segregated assets and assigned securities (R. 85). There was a provision placing property **"in trust"** with the corporation by its principal stockholders and for the distribution "to the Trustee for pro-rata distribution to the note holders" (R. 86). The books and records of the corporation were always "to be open to the inspection of the Trustee" (R. 89) and there were to be delivered to the Trustee statements of income and profit and loss annually (R. 90). The corporation was required "on request of trustee" to furnish "in detail" information as to all of its acts and it agreed to execute "further and additional instruments" as may be "required to carry out the intention of this Indenture" (R. 90). **The Trustee was vested with discretion to accelerate the entire $30,000,000 note issue in the event of default** (R. 92) **and it had further discretion in the event of such acceleration to "waive the default" and to "rescind and annul" the acceleration** (R. 92). The whole amount was payable "to the Trustee" upon demand plus its fees and expenses (R. 93). **The exclusive right of action was vested in the Trustee which was also given the right to file a proof of bankruptcy in its own name** (R. 94.) The Trustee was empowered to take any action "to prevent any impairment" of its rights and of the rights of the noteholders including "power to institute and maintain such suits or proceedings" in matters which "would be prejudicial to the interest of the noteholders" and **"No holder of any notes" was authorized "to institute any suit" at law or in equity** in respect to the powers of the "Inden-

ture'' or **"for the execution of any trusts or power"** or "for any other remedy" (R. 96). A demand for action by 25% of the note holders was conditional upon a tender "to the Trustee" of security "satisfactory to it" (R. 97). The Trustee was entitled to "receive compensation" for all services rendered by it "in the execution of the trusts" thereby "created" (R. 101). It was given a **"lien"** upon all the property for the payment of its fees (R. 101). It was empowered to release the trust instrument upon fulfillment of its conditions (R. 103).

A separate agreement was simultaneously executed (R. 105) in "fulfillment of any of the conditions on which the sale of said issue of notes was underwritten and said Trust Indenture executed" (R. 106), and the Trustee was authorized in the event of default "to institute appropriate proceedings for the enforcement thereof" (R. 110).

The $30,000,000 note issue was **sold** by a syndicate in which the Guaranty Company, a subsidiary wholly owned by the Trustee, participated (R. 16).* One class of the note holders received 50% in cash and lost $13,784,000 of their investment evidenced by the notes which were acquired by the Trustee and Morgan as a result of the exchange (R. 33). **Another class of noteholders have lost their entire investment of $1,213,000** (R. 34). Now, in a suit by a noteholder against the Trustee the court reached a conclusion that no trust relationship was ever established by reason of the foregoing matters and that the Trust Indenture was **"nothing"** as there was no trust **res** and that there was **"no such thing"** as a **trust** and (p. 2201) there is nothing upon which the trust "can be founded".

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* The Senate Report No. 714, Part 3, at page 1020, contains the underwriting agreement to float the loan at a commission of $3,500,000 to the syndicate formed by the Guaranty Company, the wholly owned subsidiary of the Trustee. Morgan was to receive for its share 20,000 in warrants (see page 1038 of the Report).

Query: What was this Trust Indenture upon which $30,000,000 in notes were floated on the market by the Trustee and by its Subsidiary, whereby over $15,000,000 were lost to the investors?

The Fundamental Law. The fundamental law of trusts was completely overlooked by the court. **The right and powers transferred from the note-holders to the Trustee, and the discretionary duties vested in the Trustee are in themselves sufficient to constitute the trust relationship.** Rights and powers are such incidents of a trust *res* as to create a trust relationship. In 65 C. J. p. 235, the author said:

> "While the subject matter of a trust must be lawful definite property, there appears to be no limitation or restriction on its kind or nature, it being the rule that a trust may exist in any property, real or personal, legal or equitable, which is in existence and which, in the eye of the court of equity, is of value. **Thus it is held that a trust may exist in a bond,** money, **promissory notes,** etc." (Boldface ours.)

That a right or power is in itself sufficient to constitute a trust **res** was squarely held by the leading authority on trusts. In Perry on Trusts, vol. 1, section 68, the author describes the properties which may become the subject matter of a trust as follows:

> "At common law no possibility, right, title nor **chose in action** could be granted or assigned to strangers. But in equity the rule is different, and **choses in action,** expectancies, contingent interests, and even possibilities may be assigned, and a valid trust created in them. Equitable reversionary interests stand upon the same ground. Property not owned by the assignor at the time, and not even **in esse,** may be assigned in equity; and **a valid trust** may be created in **a naked power or authority.**" (Emphasis ours.)
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> See also Bogert on Trusts, section 951.

In Volume 1, Section 2.2, Professor Scott points out that the characteristics of a trust indenture securing corporate bonds is completely different from the characteristics of the ordinary trust and the present Restatement of the Law of Trusts does not deal with trusts securing bond issues and that this will be covered by the future volume of the Restatement of the Law of Trusts. The use of the word "trusts" is frequently employed to indicate duties, relations, which are not strictly and technically trusts. (*Holsapple* v. *Schrantz,* 65 Ind. App. 390, 117 N. E. 547; *Stephenson* v. *Golden,* 279 Mich. 710; *Fox* v. *Greene,* 289 Mich. 179, 183.)

In Jones on Bonds and Bond Securities, Volume 2, section 1030, the author says that the nature and character of trusts assumed by corporations in security bond issues does not merely depend upon the express terms of a trust indenture "but upon the implications, as well, which arise from the relations of the parties and the condition and nature of the trust property", and in section 1053, at page 492, the author says:

> "In general, the duties of a trustee under an indenture securing the payment of corporate bonds are comparable, though not at all points parallel, to those assumed by one undertaking to perform any other trust".

The author further says at page 493:

> "There are, however, duties with which all trustees in corporate mortgages are burdened. They are not mere stakeholders, with the negligent responsibilities that attach to such an office."

Article IV of the trust indenture gave discretionary power to the Trustee to accelerate the note issue in the event of default or in the event of insolvency. Section 24 of the trust indenture (R. 94) **vested the exclusive right**

of action in the Trustee and the Trustee was even vested with the right to file a proof of debt in its own name and the company agreed to pay the Trustee's fees (R. 95). To say that an instrument of this kind lacked a **res** as to strip the instrument of the characteristics of a trust, **is to do violence to the very instrument which was drawn by Trustee.** This question was decided adversely to this contention in *Farmers Loan & Trust Co.* v. *Lake Street R. R. Co.,* 173 Ill. 439 (reversed on another point in 177 U. S. 51). On page 452 the Court pointed out that the trust instrument which vests discretionary duties in a trustee is an **active trust.**

The opinion cites (R. 156) *Bradford* v. *Chase National Bank,* 24 F. Sup. 28, on the point that there must be a trust **res** to create a valid trust. There, it said: "There must be an asset—whether it be land, a chattel or **a chose in action**—in order to have a trust of any kind, express, implied in fact, or impressed by law". **The $30,000,000 in notes constituted choses in action** and was a trust **res** establishing the trust or **fiduciary relationship between the noteholders and the Trustee.** There were certainly some rights conferred upon the Trustee and some limitations were placed upon the corporation by the trust instrument. Such **right** constituted a trust **res** (Bogert on Trusts, section 17, page 74). **A note or a bond** is a "thing" or a "**res**".

Judge Bright called the document (R. 136) "**a peculiar instrument**".* Section 16 of the trust instrument (R. 85) recites that the corporation "has obtained the execution and delivery to the trustee of an agreement by O. P. Van Sweringen and M. J. Van Sweringen with the Trustee for

* See Report No. 714, Part 3, of the Senate at page 889 under the heading "Some Things the Public Did Not Know", and under its discussion of "The Indenture".

the benefit of the holders of the note by which the Van Sweringens will jointly and severally undertake and agree that whenever from time to time the aggregate value of the unencumbered shares of the common stock of Alleghany Corporation * * * shall be less than 50 per cent" of the outstanding notes they would "repair such deficiency by assigning and delivering or causing to be assigned and delivered to the company readily marketable securities to an amount sufficient when taken at their current market value to equal the amount of such deficiency". This **contract constituted** a trust **res** (Bogert on Trusts, section 17, page 74). This agreement related to the "assigned securities" **which was not the property of the corporation** but was the personal property of the Van Sweringen brothers. **Here was a specific res which was delivered to the Trustee under the terms of the trust instrument.** The provision in the trust indenture which stated that limitations shall not be treated as a pledge or mortgage related to the "segregated assets" but **not to the "assigned securities".** It did not exclude the existence of a trust.

The Trustee **entered upon its active duties** and actively participated for the alleged protection of the noteholders (R. 48). A trustee who enters upon its duties at such a stage cannot claim that its duties were passive (*Straus* v. *Chicago Title & Trust Co.,* 273 Ill. App. 63). There it was said (p. 71):

> "It would be absurd to regard the trustee's duties as terminated at the very time when his protection was most needed".

The court therefore clearly erred in holding that there was no fiduciary relationship between the Trustee and the noteholders.

II.

The Affirmance of the Summary Judgment on the Ground That Even If There Existed a Trust Relationship Plaintiff Failed to Show Even Prima Facie That She Sustained any Loss As a Result of the Breach of Trust Because the Assets of the Company Were of Doubtful Value Is in Direct Conflict with Another Decision of the Same Circuit in Construing Rule 56 That Every Doubt Must Be Resolved Against the Movant.

The second reason for the affirmance of the summary judgment is based on the ground that even if there existed a fiduciary relationship between the parties and there was a breach of trust, petitioner did not show "even *prima facie*" that "any injury" resulted to her.

The District Court sustained the summary judgment on the ground that the Trustee and Morgan did not receive any benefits as a result of the offer (R. 141). Our brief in the Court of Appeals pointed out the benefits which the Trustee and Morgan received. The Court of Appeals was evidently satisfied that the Trustee did receive some benefits and, therefore, affirmed the summary judgment on the ground that there was no "*prima facie*" case of "injury", overlooking that there was no opportunity to offer proof as the matter was heard on the motion for the summary judgment.

The reasoning for the conclusion that there was no "injury" to the petitioner appears from the statement of the Court (R. 156, 157) that if petitioner had not accepted the offer and resorted to the "segregated assets" and "assigned securities" and realized therefrom 50% in cash, she would not have realized anything on the

deficiency for over half of the debt out of the assets of the company which consisted primarily of "a doubtful open account of the subsidiary company of $27,154,-584.03". Of course, the "open account" was **never doubtful.** What the court meant to say is that the **value** of the open account was doubtful.

In the concurring Opinion by Judge Frank he stated that he based his concurring opinion on the last paragraph and not on the other issues which "are less clear".

The matter was not decided on a **trial but on defendants' motion for a summary judgment.** The motion had to fall or stand on **its own strength** and not on any weakness in plaintiff's position.

A movant is not entitled to a summary judgment **unless the conceded facts show beyond any doubt** that the plaintiff is not entitled to *any* relief (*Clair* v. *Sears, Roebuck & Co.,* 34 F. Supp. 559). The opinion of the same circuit (*McElwain* v. *Wickwire Spencer Steel Co.,* 126 F. (2) 210) is to the same effect and is **squarely in conflict with the opinions in the instant case.** (See also *Miller* v. *Miller,* 122 F. (2d) 209, 212, construing Rule 56.)

There was nothing in plaintiff's pleading justifying a conclusion that she did not sustain damages. There was nothing in defendants' pleading relating to the claim that plaintiff did not sustain any damages. The court determined such facts from a "glance" at the balance sheet and concluded that the asset in excess of $27,000,000 consisting of the "open account" against the Cleveland Building Terminals Company was "a doubtful open account", or, in other words, **of doubtful value,** so that if the exchange was not made, the noteholders would have received in addition to the 50% in cash, **assets of a doubtful value.** Even if this be so, the defendants would

not be entitled to a summary judgment **as every doubt must be resolved in favor of the plaintiff.** However, there is no foundation for the Court's determination.

The Complaint alleged (R. 8) that it was known to the defendants that "the open account in excess of $27,000,000 was not fully collectible". The Answer of the defendants **denied** this allegation (R. 13). **Their denial can only be construed to the effect that the defendants did not know that the open account in excess of $27,000,000 was not collectible.** The Bankers who filed their sworn answer had the same balance sheet before them so that they could have had a "glance" at such balance sheet, yet they stated in their pleadings that they did not know that the $27,000,000 was not fully collectible. The Trustee and Morgan were interested in the assets of the subsidiary and the value thereof was not "doubtful" to them. They sought to prosecute their claim against the subsidiary as it appears from an appeal taken from the allowance of the claim filed by Morgan on behalf of itself and the Trustee (*Re Van Sweringen,* 111 F. (2) 378). It also appears from another appeal that Midamerica, which purchased the $13,784,000 in notes from Morgan, endeavored to establish its claim against the Cleveland Terminals Building Company and was interested to appeal from the decision of the trial court (*Re Van Sweringen,* 119 F. (2d) 231), and was also interested in applying for writ of *certiorari* to this Court, where its application was denied (314 U. S., page 671). **The claim was evidently not of doubtful value.** Incidentally, the Cleveland Terminals Building Company was reorganized; none of the mortgages were foreclosed; and the equity of the company for the benefit of its general creditors is of substantial value. Therefore, the open account in excess of $27,000,000 which would have ranked "equally" with the

claim of the Trustee and Morgan against the reorganized Cleveland Terminals Building Company (R. 42) was and is of **substantial value.** At any rate, the court was in no position to determine such value on the summary judgment for the defendants.

III.

The Respondents Were Guilty of Fraud and Violated Their Trust Duties and Under No Theory of Law Was It Proper To Sustain Their Motion for a Summary Judgment.

The Van Sweringen brothers, who controlled the entire empire, were fiduciaries of the noteholders, the creditors of the company, in view of the insolvency of the company. (*Younglove* v. *Lima Co.,* 49 O. S. 663; *Thomas* v. *Matthews,* 94 O. S. 32, 47). The "offer" operated for the personal benefit of these fiduciaries as well as for the benefit of the Trustee and Morgan. Even if there was no trust relationship between the Trustee and Morgan and the noteholders, they were in the capacity of fiduciaries under the rule that if third persons enter into agreements with fiduciaries resulting in benefits to the fiduciaries, **such third persons stand in the capacity of fiduciaries** and must account for the profits realized by the fiduciary. This doctrine was recognized by the District Court (R. 142) which cited *Irving Trust* v. *Deutsch,* 73 F. (2) 121. See also *Re Van Sweringen Corporation,* 119 F. (2) 231, 234. However, the Trustee and Morgan **directly benefited** from the transaction, which resulted in **loss** to the plaintiff.

The total amount of the "segregated assets" and "assigned securities", according to the "offer" (R. 71) aggregated $13,440,681.86. Based on the outstanding

notes of $26,234,000 and accrued interest of $787,290.00 there was required in "segregated assets" a total of $13,894,290 so that there was a deficiency in such assets in the amount of $453,618.20 which the Van Sweringens were obligated to make good.

If they did not supply this deficiency, the Trustee had the right to accelerate the entire note issue. In such event all of its "segregated assets" and "assigned securities" would have been applied in part payment of the $26,234,000 notes. The note holders would have then received 50% in cash out of the "segregated assets" plus a deficiency for the balance. **They could have resorted then to the remainder of the assets of the Van Sweringen Corporation** consisting of the entire capital stock of the subsidiary which they **scheduled at cost in excess of** $29,000,000 (R. 64) and they could have resorted to the enforcement of the **"open account" against the Subsidiary in excess of** $27,000,000 (R. 64). Such a procedure would not have been in the interest of the **fiduciaries,** the Van Sweringens, the "Guaranty Trust" and its partner in the loans, Morgan. This would have thrust the Subsidiary into bankruptcy in 1931, and they would not have been in position to manage and operate up to 1936 when they finally landed in bankruptcy.* Morgan and Guaranty Trust Company, **who were behind the scene, made the "offer" possible.** The Van Sweringen Corporation and its officers were their **agents,** and **they,** the defendants, the **undisclosed principals,** are liable to the plaintiff for the damage caused to her in exchanging her notes for the worthless stock which **they supplied.**

* It should be noted that the Van Sweringens managed to receive $100,000 annually from 1931 to 1936 and that they had a direct personal gain to such extent (Re Van Sweringen, 119 F. (2) 231).

Morgan and Guaranty Trust Company Exchanged the Worthless Stock for the Notes.

All common stock of the Van Sweringen Corporation was pledged as collateral under the note which was jointly owned by Morgan and Guaranty Trust Company. They participated in bringing about the "offer" which enabled them to substitute the pledged worthless common stock for $13,784,000 notes of the $30,000,000 note issue (R. 33).* It is **they who received plaintiff's $5,000.00 notes and gave in exchange therefor the 200 shares, which they knew to be worthless.** In order to accomplish this exchange **they** caused the balance sheet to be made up which showed the value of the common stock to be $32,773,638.28 (R. 65).** **They knew that the stock was valueless.** This is confessed by the affidavit which states that a "study" of the balance sheet revealed such facts (R. 40). **They did not disclose the result of their study and analysis to the plaintiff in the "offer" that they caused to be submitted to her. They did not disclose to her the fact that the corporation had no funds to meet the interest payments and if bankruptcy followed the stock would be worthless, which facts were known to them as is shown by the affidavit** (R. 43). On the contrary, the form of the "offer" which **they** prepared stated that interest would be paid in the **"usual"** way at the office of the Guaranty Trust Company (R. 72, 73). **This led the noteholder to believe that the corporation was in good standing and that the stock had some value.**

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* The form of the offer was prepared as part of the agreement with Morgan as Exhibit "A" (R. 123, 126). This offer stated (R. 72) that this balance sheet "will be furnished on request".

** The defendants were clearly liable under the rule that where two persons who occupy a fiduciary relation to a third person enter into a transaction with "each other" whereby one of their agents acquires the property of the third person "to his own advantage", such transaction is "contrary to public policy" and is "prima facie fraudulent" (Rothman v. Wilson, 9 Cir., 121 F. (2) 1000).

In order to arrive at the valuation of the stock in excess of $32,000,000 it was necessary to show in the balance sheet the investment in the subsidiary at **cost** in the amount of $29,253,066.30 and to include the "open account" against the subsidiary in the face amount of $27,154,584.03 (R. 64). This was done in **violation of the terms of the trust indenture** which provided that values were to be carried at "**existing market value**", or at "**fair value**" when no market was available (R. 83). It is true that the balance sheet contained in **small type** (R. 66) in footnote 2 the market value of the securities. **These marginal notes are hardly understandable to the average investor.** No fair value of the real estate was given. **They featured the value of the capital stock in large capital letters** (R. 65). While the expert banker might, as a result of a "**study**" and "analysis" of the balance sheet, **detect** that the corporation was insolvent, **as they did** (R. 40), and while the Judges of the Court of Appeals were able to ascertain such facts from a "glance" at the balance sheet, the average investor could not be expected to do that. Plaintiff, according to her testimony, was not a business woman and **did not understand the balance sheet** (R. 55) **and was of the opinion that she was getting value when she received the stock** (R. 57). She said, "**I assumed that the stock was worth half of my notes because they gave me half money and half stock. It was half and half**" (R. 57). The depositions which defendants offered in support of the summary judgment were **conclusive on them.** Morgan and Guaranty Trust Company had actual knowledge that the stock was worthless.* **They entered into an agreement to publish the offer** for the benefit of the Van Sweringens and for their own

* The fact that the "victims" might have "discovered the cheat" is immaterial when the parties did not have equal means of knowledge (Falter v. U. S., 23 F. (2) 420, C. C. A. 2).

benefit, and **concealed the true facts.** They cannot escape liability for such conduct.

In discussing another phase of the situation involving the subject of the sale of the same $13,784,000 notes by Morgan on September 30, 1935, to Midamerica, a corporation organized by the Van Sweringens, the Sixth Circuit said *In re Van Sweringen Corporation,* 119 Fed. (2) 231, at page 234:

> "It seems soundly settled that one who knowingly joins a fiduciary in purchasing for profit the property of the trust estate in unlawful circumstances, became jointly and severally liable with him for the resultant profit."

Here, not only did Morgan join with the Van Sweringens for their own benefit, but also for the benefit of the Guaranty Trust Company **to obtain the exchange of the pledged worthless stock for the 13,784,000 notes** to be held as security under the joint note of Morgan and Guaranty Trust Company. Their liability is not only based on the benefits resulting to Van Sweringens as fiduciaries, but on the personal benefit which **they derived out of the fraudulent transaction.** Van Sweringens and the Corporation were their instrumentalities or agencies to make the offer under the agreement. They, the defendants, concealed these material facts from the plaintiff, and **the concealment of these facts constituted fraud in equity.**

The opinion of the District Court says (R. 142):

> "We can, however, **assume there was a trust relation,** and apply the now oft-quoted statement of Chief Judge Cardozo that, **'A trustee is held to something stricter than the morals of a market place,'** and that 'Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by "disintegrating erosion" of particular exceptions.' (*Meinhard* v. *Salmon,* 249

N. Y. 458, 464). **One who joins with a fiduciary in a breach of trust is also responsible.** *Jackson* v. *Smith,* 254 U. S. 587-589. *Irving Trust Co.* v. *Deutsch,* 73 F. 2, 121, cert. denied, 294 U. S. 708."

After stating this rule, it said:

> "There still remains the question whether there was such action on the part of the defendants which made them liable to the plaintiff. They did nothing the trust indenture forbid. **They did substitute in their collateral the balance of the notes for the stock of the Company.** What the stock was then worth was problematical. Both sides now admit that it was worthless, but who could then tell?"

The Court of Appeals while it affirmed the decision answered the question by saying that it could tell then that the stock was valueless (R. 156).

The affidavit of the defendants in support of the summary judgment also stated that the analysis of the balance sheet of September 30, 1931, showed that the stock was worthless (R. 40). Whether plaintiff understood the balance sheet, as she said she did not (R. 55), may be open to question, but certainly **the persons who prepared the balance sheet, who analyzed it and who were the bankers who floated these loans—they knew the real facts and that the stock was worthless** (R. 40). **They had no right to unload on the noteholders the worthless stock which they held, in exchange for the valuable notes which the noteholders owned.**

The opinion of the District Court stated (R. 142) that the defendants were seeking "to avoid the demolition of the Van Sweringen empire for the benefit of all concerned" and they insured payment to the plaintiff "more than the then market value of the stock" (notes.)* The

* The motive of the Trustee is no defense for the breach of a trust (White v. Sherman, 168 Ill. 589).

District Court asked: "Was there a breach of that high degree of good faith which the law requires of a fiduciary?" It answered: the Trustee could have said "No" and had it taken that position the plaintiff would not have benefited from such a position. It says that the Company might have been able to finance the payment of interest, thereby preventing the default, and used the "segregated assets" to purchase the notes at market prices which declined until it had 50% of the notes, when the Company could have released the "segregated assets". The Court of Appeals was also influenced by such an argument (R. 156). **A Court may not assume a condition different from what the facts were,** particularly on a motion for a **summary judgment when every assumption must be in favor of the person against whom the summary judgment is entered.** The facts as they appear were that the corporation was unable to raise the $900,000 in interest (R. 27). The "offer" which they made on October 30, 1931, was only **one day** before the interest was due—November 1, 1931. How was it possible for the company to raise in one day the required interest and to accomplish such a miracle? **There is also no proof that the noteholders would have sold $15,000,000 notes at a declined market. Failure to obtain $15,000,000 notes would have prevented the release of the "segregated assets". The court had no right to assume a state of facts which might not have accrued in order to defeat the cause.**

The District Court said (R. 143) that bankruptcy might have followed and plaintiff would have had a claim "as a general creditor". It overlooked that **there was no possible chance for a bankruptcy to be instituted** against the Van Sweringen Corporation. The noteholders were the **only** creditors (R. 65). True, the Van Sweringens were also creditors to the extent of $10,178,506.54, but their

notes were **subordinated** to the note issue and did not mature until "May, 1935". There was also a **contingent** claim of $8,000,000 (R. 65) but this **contingent creditor could not have instituted a bankruptcy proceeding** (*Re Howell,* 215 Fed. 1, C. C. A. 2; *Re The Literary Digest,* 105 F. (2) 957; *Manhattan* v. *Irving Trust Co.,* 291 U. S. 320).

The only existing creditors who could have maintained insolvency proceedings were the noteholders but **their notes were not due and the right to accelerate as well as the right to commence any action was exclusively vested in the Trustee. The Trustee was the only party who could have maintained an action to obtain judgment on the $30,000,000** note issue, to appropriate the "segregated assets" and "assigned securities" to satisfy one-half of the debt, to obtain a deficiency judgment for the balance, and enforce it against the assets of the Van Sweringen Corporation which consisted of its stock in the subsidiary at an investment of $29,000,000 and to the "open account" against the subsidiary in excess of $27,000,000. This was not in the interest of the Trustee and Morgan, who were creditors of the subsidiary to the extent of $11,000,000 each because **the noteholders would "rank equally" with them as creditors of the subsidiary** (R. 42). **This is why the Trustee and Morgan caused the offer to be submitted in the name of the Van Sweringens,** but in reality for their own benefit. **This came from their own mouth.** Mr. Shriver stated in his affidavit (R. 42):

> "So far as concerned the New York Banking Group (Guaranty Trust and Morgan) * * * if there were a deficiency in the collateral (under the $23,500,000 note) after a forced sale * * * this claim (of the Trustee and Morgan) **would rank equally with Van Sweringen Corporation's claim for approximately $27,000,000 against Cleveland Terminals Building Corporation.**"

Here was **the real motive** behind the "offer" to prevent this $27,000,000 claim, by excluding the noteholders as **creditors,** and relegating them to the position of **stockholders.**

It was asserted below that the moving consideration for the offer was "to stop the private purchase of notes by the Van Sweringen Corporation with the 'segregated assets'" which was permissible under the terms of the indenture and the opinion seems to have adopted such view (R. 156). **If they really wanted to stop the purchase of these notes at 30 cents on the dollar they could have notified the noteholders that there was available for them 50 cents on the dollar from the "segregated assets" besides the remainder of their pro rata share in the $69,000,000 worth of assets of the corporation for the remainder of the 50 per cent.** A noteholder who would have received such information would not have sold his notes for 30 cents on the dollar. It was necessary to acquire $15,000,000 of the notes in order to release the "segregated assets". **Certainly $15,000,000 in notes could not have been acquired at 30 cents on the dollar if the Trustee had given the information to the noteholders that more than 50 cents per dollar was available for them.***

Why was the Guaranty Trust Company so alarmed (R. 24) if it be true that there was no trust relationship, that there was no responsibility upon it and that its trust was mere routine? The answer is plain. The Trustee knew from its "study" that the Van Sweringen Corporation was then insolvent. The Trust agreement provided (R. 91) that in the event of insolvency or in the event the company shall admit its inability to pay its debts when

*In fact the bankers threatened the Van Sweringens with such action and obtained their commitment that they would not purchase the notes as shown in Senate Report No. 714, Part 3, pp. 974-975.

they became due that the Trustee may declare the entire amount due and take the proper action, and it provided that in such event (R. 93) that the Trustee was then to act **"as a trustee of an express trust"**. The Trustee was also not unmindful of the fact that its position was then **adverse and delicate.** That is why it was **alarmed** and **it was its duty to at least disclose the information to the noteholders.**

IV.

The Fraudulent Offer to Exchange Was Not the Offer of the Van Sweringens But the Offer of the Respondents, Morgan and Guaranty Trust Company, and It Is They Who Committed the Fraud and Breach of Trust.

The "offer" which was submitted to the plaintiff as well as to the other investors was ostensibly an offer of the Van Sweringen Corporation. **In reality it was the offer of Morgan and the Guaranty Trust Company.** Morgan entered into the **secret** agreement to transmit the offer to the public (R. 119). The form of the offer was incorporated in the agreement (R. 70, 126). Morgan and the Guaranty Trust Company **undertook to make the common stock available for the exchange under the offer.** It is **they** who had the common stock as security for the collateral. **It is they who wanted to exchange the pledged worthless common stock for the valuable notes** and who **obtained such notes.** It was they who concealed the true facts and who **obtained the benefits resulting from the offer.**

The affidavit of Whitney states that Morgan and the Guaranty Trust Company each loaned $11,000,000 as part of the $39,500,000 loan which was made to save the Van Sweringen "Empire". The common stock was placed with Morgan as security for such loans. The affidavit further states (R. 28) that a conference was held with

the Bankers in which Morgan and the Guaranty Trust Company participated and that **as a result of these conferences "these general terms having been worked out among the parties named,"** the Van Sweringen Corporation prepared the terms of an offer of purchase for noteholders. It also states **that this offer was examined by Whitney and "by officers of Guaranty Company of New York and of Guaranty Trust Company of New York"** (R. 20). This "offer" was made a part of the secret agreement (R. 126). **The Guaranty Trust actually participated in the preparation of the offer** (R. 48, 49). It is, therefore, obvious that this "offer", which was made ostensibly in the name of the Van Sweringen Corporation, **was in reality the offer of Guaranty Trust and Morgan,** who were the **undisclosed** principals and stood behind the scene. The Van Sweringen Corporation was their tool and instrumentality, and the Trustee and "Morgan", as undisclosed principals who received the benefits, are clearly liable (*Adams* v. *Collier,* U. S., 8 Cir., 73 F. (2) 975, 977).

(a) Where an Agent Perpetrates a Fraud on a Third Party for the Benefit of His Undisclosed Principal, the Third Party May Sue the Principal Upon the Disclosure.

A reading of the secret agreement of "Morgan" (R. 119) and a study of the facts as they are revealed from the affidavits, as discussed above, demonstrates that the Van Sweringen Corporation was the instrumentality and **agent** of Guaranty Trust and Morgan to obtain the exchange of the worthless pledged stock for the valuable note to be substituted as collateral for their personal gain. Van Sweringen Corporation, **their instrumentality,** did not disclose in the offer which the Trustee and Morgan prepared that it was acting for Morgan and Guaranty Trust. On the contrary, it was stated in the offer

(R. 71-2) that "the stock to be delivered to the noteholders * * * will be furnished by the Van Sweringen interests." This statement either referred to Morgan and the Guaranty Trust as synonymous with "Van Sweringen interests" or was a deliberate misrepresentation as the stock was to be delivered under the secret agreement by Morgan (R. 122). **It was Morgan and the Guaranty Trust Company which caused the misleading offer to be mailed to all noteholders including the plaintiff.*** It is **they** who prepared the "offer" which stated (R. 72) that "the notes acquired after the retirement of $15,000,000 will be acquired, not by the corporation, but by the Van Sweringen interests." Why did they not state that this will be acquired by Morgan and the Trustee, whose duty it was to protect the noteholders? Why did they use the words "Van Sweringen interests" instead of "Morgan and Guaranty Trust"? **Because of their adverse interests and fiduciary relation it was their duty to speak,** particularly when they had actual knowledge that the stock which they were going to exchange for the notes was worthless,** and that it was done for the purpose of avoiding the bankruptcy of the subsidiary which would greatly affect the interest of Morgan and the Trustee as its creditor. The fraud of the Van Sweringen Corporation was **their fraud,** as the Van Sweringen Corporation **was their agent** and they, Morgan and the Trustee, were the undisclosed principals. Upon the disclosure of the undisclosed principals the plaintiff, as well as the other noteholders, were entitled to recover from the undisclosed principals.

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* One who knowingly and intentionally clothes another with power to commit a fraud, and knowing that such fraud is being committed, remains silent, is liable (Raymond v. Sec. Realty Co., 91 F. (2) 163, 172).

** Where duty to "speak" exists, suppression of truth is actionable (Kershaw v. Julien, 32 F. (2) 528).

In *McIntire* v. *Pryor,* 173 U. S. 38, 52, the rule was announced that where frauds are committed by an agent in procuring title to property for the benefit of its principal the principal is chargeable therewith in the same manner as if he had committed them personally. The authorities are collected in 2 Amer. Jur. Sections 393, 394. See also Restatement of the Law of Agency, Section 188.

It should also be noted that the Company was actually insolvent at the date of the offer. Being insolvent, it was then Trustee for its creditors. In making the offer to its creditors it was the duty of the Company to disclose all material facts. The defendants who caused the offer to be made by the Company and who were instrumental in having it conceal the facts from the plaintiff and the other creditors and who derived a benefit therefrom are, therefore, clearly liable. (*Conner* v. *Craig,* 4 Cir., 216 Fed. 729.)

(b) Even If the Offer Was That of the Van Sweringens the Defendants Who Ratified the Offer and Accepted the Benefits Therefrom Are Liable.

The affidavit of Shriver stated (R. 39) that the banking group, which included Morgan and "Guaranty Trust," was in position "to throw the borrowers into bankruptcy" by calling the loans if the interest was not paid by November 1, 1931, and that the "borrowers" were in no position to pay such interest. The "study" of the balance sheet of the "parent" and its "subsidiary" disclosed to them that both were insolvent (R. 40). In the event of bankruptcy **the noteholders would not have received half of their debt** according to this affidavit (R. 43). The conclusion that **they** reached that the "assigned securities" and "segregated assets" would not be sufficient to pay half of the $30,000,000 note issue **was clear**

knowledge on their part that the common stock of the Van Sweringen Corporation **was worthless.** With knowledge of such facts they permitted the offer to be made, and **accepted the benefits therefrom in exchanging their worthless collateral for the valuable notes.** Under such circumstances they are clearly liable (*Paige* v. *Keeves,* 362 Ill. 64, 74; *Goldsmith* v. *Koopman,* 152 Fed. 173; *Great Lakes Towing Co.* v. *Mills Trans. Co.,* 6 Cir., 155 Fed. 11, 21).

(c) The Fact That Neither Morgan Nor Guaranty Trust Personally Defrauded the Plaintiff Is No Defense.

There are some references in the affidavits that the plaintiff has admitted by her depositions that she received no communications from either Morgan or from the Trustee and that she admitted that the defendants did not personally defraud her. This is no defense to the action, as the act of their agent is the act of the principal, and when plaintiff discovered the undisclosed principals when she was invited by the original plaintiff to join as a party (R. 74) she was entitled to sue and to recover.

In *Zimmern* v. *Blount,* 238 Fed. 740, the Court said (p. 743):

> "Nor is it necessary that a fraud be personal to the defendant. It is sufficient if committed by his agent and he profit by it."

See also *United States* v. *Carbon County Land Company,* 46 Fed. (2) 980, 987.

In *Brach* v. *Moen,* 35 F. (2) 475 (Certiorari denied 280 U. S. 613), the rule was thus stated:

> "One who **accepts the fruits of fraud** with knowledge of the misrepresentations or **concealment** by which they were obtained will be held liable thereafter, **even though he did not personally participate in the fraud.**"

(d) The Real Purpose of the Offer Was to Avoid the Collapse of the Van Sweringen Empire Wherein Morgan and the Guaranty Trust Company Were Personally Interested and Not to Save the Investment of the Noteholders.

Throughout the affidavits there is the assertion that the motive of Morgan and of the Trustee was to avoid bankruptcy of the Van Sweringen Corporation and to apply all of the "segregated assets" and "assigned securities" for the exclusive benefit of the noteholders. We have shown above that no bankruptcy was possible and that this was not the motive. The real purpose was to avoid the bankruptcy of the "borrowers" whereby Morgan and Guaranty Trust Company stood to lose their $22,000,000 (R. 42). The Guaranty Trust Company and Morgan participated in the scheme to prevent the bankruptcy of "Vaness," whose $16,000,000 note it held and the bankruptcy of the Subsidiary which owed them $23,500,000, and which companies were unable to meet the interest payment which was due November 1, 1931. The real purpose was to prevent an acceleration of the note issue whereby the noteholders would have received all of the "assigned securities" and "segregated assets" in satisfaction of one-half of the note issue, and they would have received a deficiency decree for the balance, whereby they were able to enforce the open account in excess of $27,000,000 against the subsidiary, which owed Morgan and Guaranty Trust Company $23,500,000. **This is what they sought to avoid and what they did avoid.**

(e) It Was the Duty of the Trustee to Protect the Interest of the Noteholders Which It Failed to Do Because of Its Adverse Interest.

The Guaranty Trust Company, The Trustee under the note issue, entered into an agreement with Van Sweringens "for the exclusive protection of the $30,000,000 note issue" (R. 105). The agreement provided that the securities be held by the corporation in "**trust**" for the noteholders. Under the terms of the agreement the Trustee had the "exclusive" right of action to enforce the agreement. The Trustee, according to the affidavits, was a party to the secret agreement between Morgan and the Van Sweringens to prevent the acceleration and misapplication of the "segregated assets". It had knowledge that the corporation had no funds to meet its interest payment on November 1, 1931 and that a secret agreement was made to circumvent the application of the "segregated assets". It actively participated in such a scheme. It cannot escape liability. As Trustee of the note issue it had the power to accelerate the note issue and to resort to the "segregated assets" and "assigned securities" and to obtain a deficiency decree against the remainder of the assets. It participated in a deal whereby the "segregated assets" and "assigned securities" were used for the personal benefit of the Van Sweringens, Morgan, and itself. The noteholders were eliminated as creditors and Morgan and the Trustee were enabled to acquire over $13,784,000 in notes **to become the sole creditors of the Van Sweringen Corporation** and to receive the excess money from the "assigned securities" in application of a debt due from "Vaness". This was a breach of trust duties and obligations and they are liable for such breach. *New York Trust Company* v. *Michigan Traction Co.*, 193 F. 175.

Because of the adverse position of the Trustee it was its duty to either **resign,** or to **disclose** all the information to the noteholders. Whether or not bankruptcy or insolvency would have produced more or less than 50c on the dollar is of no importance. **The noteholders had the right to know the real truth and to determine for themselves what was best, when the Trustee** (who was selected to protect their interest) was not able to give the protection because of its **adverse** position. The fact that the Trustee lent its aid by loaning $11,000,000 in 1930 to make good the "segregated assets" in order to avoid the collapse of the entire Van Sweringen Empire is of no importance. **The fact is that in 1931 there were sufficient assets in the "segregated assets" to pay 50% to the noteholders.** The Trustee derived the benefit in that it avoided insolvency proceedings against the **top** holding company, Vaness, the **holding** company, Van Sweringen, and its **subsidiary,** Terminal, in selling the collateral prior to **such insolvency proceedings,** in obtaining its allowance of a claim in excess of $27,000,000 and **eliminating the noteholders as creditors.** The Trustee **personally benefited from the exchange** in that it received over $13,000,000 in notes in exchange of the **worthless stock** which it held as collateral. It, therefore, violated its trust duties to gain personal benefit and it is liable for such breach of trust.

V.

Federal Courts May Take Judicial Notice of Official Reports of Congressional Committees, and the Official Report of the Congressional Committee Conclusively Demonstrates the Fraud, the Violation of the Trusts, and the Damage Sustained.

Subsequent to the rendition of the opinion by the District Court plaintiffs' counsel received the official printed copy of Report No. 714, Part 3, on S. Resolution 71 of the 74th Congress dealing with the particular subject matter. The District Court was asked to reconsider its opinion in the light of the Report or to allow the case to be reopened.

The court failed to consider it when it entered its final judgment. A motion was made in the Circuit Court of Appeals for leave to file the Record. The Circuit Court of Appeals denied the motion on the ground that this Report was not made a part of the Record (R. 153). We cannot see how we could have made it a part of the Record when the Report was submitted to the court after it had rendered the opinion, and when it thereafter entered the judgment there was no opportunity to make this Report a part of the Record. We asked leave of the Circuit Court of Appeals to consider the Report but it refused. It is our position that the official report of the Senate Committee may be judicially noticed without making it a part of the Record. This Court considered the official report of a Senate Committee in *Arizona* v. *California*, 283 U. S. 423. It also received similar reports in *Tempel* v. *United States*, 248 U. S. 121, and this Court may now consider this Report.

In Chapter XV, pp. 871-906 of the Report, the floating of the $30,000,000 note issue is described in detail, with the active participation of the Guaranty Trust Company, and there is attached thereto the underwriting agreement wherein the Guaranty Company of New York, its wholly owned subsidiary, undertook to sell the notes at a consideration of $3,500,000 in commission (See page 1020 of the Report). In order to evade the various Blue Sky Laws of the states they resorted to placing the bonds on the Exchange. In addition to the $3,500,000 in commissions, J. P. Morgan & Co. was to receive 20,000 in warrants for its share (See page 1038). Chapter XXIV deals with the 1930 crisis leading up to the loan of the Guaranty Trust and Morgan in the amount of $22,000,000 (pp. 907-930). The rescue loan is described in Chapter XXVIII, pp. 931-958, and the "1931 crisis" which lead to the "offer" whereby the noteholders were defrauded to the extent of over $15,000,000 is vividly described in Chapter XXVIII, pp. 959-987. A reading of this Report will convince this Court of the justice of our cause.

For the reasons above stated we respectfully submit that the writ of *certiorari* be issued.

Respectfully submitted,

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